The State Bar of California

Client Trust Accounts and Bank Stability Concerns

FAQs

1) **Q: How does FDIC insurance protect client trust funds?**

A: Selecting a bank that is regulated by a federal or state agency and that carries deposit insurance from an agency of the federal government is an important consideration. As your client's fiduciary, you are responsible for protecting your client funds.

Based on emergency legislation, effective October 3, 2008 through December 31, 2009, FDIC insurance has been raised from $100,000 to $250,000 for certain funds on deposit. In the case of your IOLTA account, provided the fiduciary nature of the account is disclosed in the account title and you keep required records in good faith and in the regular course of business, each of your client's funds may be separately insured up to $250,000.

However, the per-client limit may include all of the funds that your client has on deposit at that bank. For example, if you are holding $150,000 for a client at a certain bank, and the client has another $150,000 on deposit at the same bank, depending on the nature of the accounts, only $250,000 of the $300,000 the client is holding in the bank is covered. The FDIC's Web site has additional information about FDIC insurance.

In addition, even if all your clients' funds are covered by insurance, by the time the FDIC pays your client his or her money, your client's interests might be adversely impacted.

For example, the delay may result in a missed a business opportunity. Similarly, the FDIC coverage will not help you if your bank goes under and you need to get copies of your client trust bank account records.

2) Q: Isn't FDIC insurance an express requirement for IOLTA deposits?

A: Effective January 1, 2008, Business and Professions Code Section 6213 was amended to define an IOLTA account as an account or investment product that is:

1) an interest-bearing checking account;

2) an investment sweep product that is a daily (overnight) financial institution repurchase agreement or an open-end money-market fund; or,

3) any other investment product authorized by the California Supreme Court.

Consistent with that legislation, the California Supreme Court rescinded its 1982 order that previously required IOLTA accounts be held in an institution that has its deposits insured by the federal government.

The legislation provides for strictly defined conservative safe investment sweep products, which are sometimes held on the investment side of the bank and therefore are not necessarily covered by the FDIC.

The Court's new order is silent on federal insurance for deposits, but the State Bar is working on regulatory requirements with respect to financial institutions either through rule or revised legislation. Monitor the IOLTA pages on the State Bar's Web site for ongoing developments.

3) Q: Given the limits on FDIC insurance, should I attempt to divide-up deposits among several banks?

A: The State Bar's Ethics Hotline is not aware of any authority in California mandating this approach as an absolute disciplinary standard. Prudence and good client communication should be exercised in electing to take this approach.

Rule 3-500 of the Rules of Professional Conduct requires a lawyer to keep a client reasonably informed about "significant developments" and the approach of dividing deposits may be something to consider with a particular client given that client's specific situation.

However, depending on the number of banks and clients involved, this approach could lead to accounting and record-keeping challenges.

Bear in mind that the goal is to maintain client funds in a financially stable institution and that FDIC insurance for a deposit is one factor to consider but it is not determinative. *(See the above discussion of investment sweep products for IOLTA deposits.)*

The FDIC has a Web page with links to several private bank rating services; however, the list is not to be construed as an endorsement or confirmation of the information provided by any of the listed companies.

In addition, you should realize that civil liability is a separate concern from State Bar disciplinary or regulatory standards. You may want to contact your professional liability insurance carrier for guidance on the pros and cons of attempting to divide-up trust fund deposits.

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